

The Accounting Officer  
Private Bag X3  
Hope Town  
Church Street  
8750

Date: 30 November 2015

Reference: 21437REG14-15

Dear Sir

**Report of the Auditor-General on the financial statements and other legal and regulatory requirements of Thembelihle Local Municipality for the year ended 30 June 2015**

1. The above-mentioned report of the Auditor-General is submitted herewith in terms of section 21(1) of the Public Audit Act of South Africa read in conjunction with section 188 of the Constitution of the Republic of South Africa section 121(3) of the Municipal Finance Management Act of South Africa.
2. We have not yet received the other information that will be included in the annual report with the audited financial statements and have thus not been able to establish whether there are any inconsistencies between this information and the audited financial statements and the reported performance against pre-determined objectives. You are requested to supply this information as soon as possible. Once this information is received it will be read and should any inconsistencies be identified these will be communicated to you and you will be requested to make the necessary corrections. Should the corrections not be made we will amend and reissue the audit report.
3. In terms of section 121(3) of the MFMA you are required to include the audit report in the municipality's annual report to be tabled.
4. Until the annual report is tabled as required by section 127(2) of the MFMA the audit report is not a public document and should therefore be treated as confidential.
5. Prior to printing or copying the annual report which will include the audit report you are required to do the following:
  - Submit the final printer's proof of the annual report to the relevant senior manager of the Auditor-General of South Africa for verification of the audit-related references in the audit report and for confirmation that the financial statements and other information are those documents that have been read and audited. Special care should be taken with the page references in your report, since an incorrect reference could have audit implications.

- The signature *Auditor-General* in the handwriting of the auditor authorised to sign the audit report at the end of the hard copy of the audit report should be scanned in when preparing to print the report. This signature, as well as the place and date of signing and the Auditor-General of South Africa's logo, should appear at the end of the report, as in the hard copy that is provided to you. The official logo will be made available to you in electronic format.

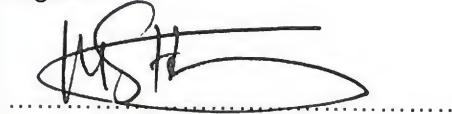
6. Please notify the undersigned Senior Manager well in advance of the date on which the annual report containing this audit report will be tabled.

7. Your cooperation to ensure that all these requirements are met would be much appreciated.

Kindly acknowledge receipt of this letter.

Yours sincerely

Signed



Senior Manager NCBU: Senzosenkosi Mthembu  
Enquiries: Eunice Ramarumo  
Telephone: (053) 836 8800

# Report of the auditor-general to the Northern Cape provincial legislature and the council on Thembelihle Local Municipality

## Report on the financial statements

### Introduction

1. I have audited the financial statements of Thembelihle Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2015, the statement of financial performance, statement of changes in net assets, and cash flow statement and the statement of comparison of budget and actual amounts for the year then ended, as well as the notes, comprising a summary of significant accounting policies and other explanatory information.

### Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with South African Standards of Generally Recognised Accounting Practice (SA standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2014 (Act No. 10 of 2014) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

### Auditor-general's responsibility

3. My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with International Standards on Auditing. Those standards require that I comply with ethical requirements, and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified audit opinion.

## **Basis for qualified opinion**

### **Operating expenditure**

6. During 2014, I was unable to obtain sufficient appropriate audit evidence for general expenditure. Consequently, I was unable to determine whether any adjustment to expenditure stated as R12 098 278 was necessary. My audit opinion on the financial statements for the period ended 30 June 2014 was modified accordingly. My opinion on the current period's financial statements is also modified because of the possible effect of this matter on the comparability of the current period's figures.

### **Revenue from non-exchange transactions**

7. The municipality did not recognise revenue from fines in accordance with the SA Standards of GRAP 23, Revenue from non-exchange transactions and IGRAP 1, applying the probability test on initial recognition of revenue. Fines were recognised before the transaction date when the municipality had no enforceable right to revenue and thus were overstated by R1 121 895 and receivables from non-exchange transactions were overstated by the same amount. In addition, I was unable to obtain sufficient appropriate audit evidence for fines revenue from non-exchange transactions in 2014 stated at R 923 798 in note 25 as it was impracticable to do so. Consequentially, there was an impact on the surplus for the year and accumulated surplus.

### **Receivables from non-exchange transactions**

8. During 2014, the municipality did not recognise all items of receivables from non-exchange transactions in accordance with GRAP 1 Presentation of Financial statements as the amounts per the Annual Financial Statements and the Trial Balance varied. Consequently, I was unable to determine whether any adjustments relating to receivables from fines in the financial statements were necessary. My audit opinion on the financial statements for the period ended 30 June 2014 was modified accordingly. My opinion on the current period's financial statements is also modified because of the possible effect of this matter on the comparability of the current period's figures.
9. Additionally, Fines were recognised before the transaction date when the municipality had no enforceable right to revenue and thus fines receivables were overstated by R1 121 895. I was not able to determine the impact on the net carrying amount of receivables from non-exchange transactions in note 12 stated at a net of R 478 369 as it was impracticable to do so. Consequentially, there was an impact on the surplus for the year and accumulated surplus.

### **Irregular expenditure**

10. Section 32 of the Municipal Finance Management Act requires disclosure of the particulars of any irregular expenditure incurred by the municipality. The audit revealed various transactions which were in contravention to the supply chain management, resulting in irregular expenditure being understated by R 797 062 (2014: R2 508 973).

## **Qualified opinion**

11. In my opinion, except for the possible effects of the matters described in the basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the Thembelihle Local Municipality as at 30 June 2015 and its financial performance and cash flows for the year then ended, in accordance with SA standards of GRAP and the requirements of the MFMA, and DoRA.

## **Emphasis of matters**

12. I draw attention to the matters below. My opinion is not modified in respect of these matters.

## **Restatement of corresponding figures**

13. As disclosed in note 50 to 51 of the financial statements, the corresponding figures for 30 June 2014 have been restated as a result of errors discovered during 2015 in the financial statements of the municipality at, and for the year ended, 30 June 2014.

## **Material underspending of the conditional grant**

14. As disclosed in note 16 of the financial statements, the municipality materially underspent conditional grants allocated for capital expenditure to the amount of R 6 785 456 (2014: R 11 620 201). This had a negative impact on service delivery in the municipality and on the construction of capital projects aimed at improving service delivery.

## **Unauthorised expenditure**

15. Unauthorised expenditure incurred during 2014 -15 was disclosed as R14 904 549 (2014: R12 606 468) in note 55 of the financial statements. This unauthorised expenditure must still be investigated and reported to council. The unauthorised expenditure was still awaiting authorisation or to be written off.

## **Material losses**

16. As disclosed in note 60 and 61 to the financial statements, material losses were reported at 58% (2014: 52%) and 39% (2014: 42%) incurred as a result of distribution losses relating to unaccounted water and electricity, respectively.

## **Going concern**

17. The financial statements indicates that Thembelihle Local Municipality is experiencing financial difficulties as current liabilities exceeded its current assets by R 43 407 622. These conditions indicate the existence of a material uncertainty that may cast significant doubt on the municipality's ability to operate as a going concern.

## **Additional matters**

18. I draw attention to the matters below. My opinion is not modified in respect of these matters.

## **Unaudited supplementary schedules**

19. The supplementary information set out in appendix A to F does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion thereon.

## **Unaudited disclosure notes**

20. In terms of section 125(2) (e) of the MFMA the municipality is required to disclose particulars of non-compliance with the MFMA. This disclosure requirement did not form part of the audit of the financial statements and accordingly I do not express an opinion thereon.

## **Report on other legal and regulatory requirements**

21. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report findings on the reported performance information against predetermined objectives for selected objectives presented in the annual performance report, compliance with legislation and internal control. The objective of my tests was to identify reportable findings as described under each subheading, but not to gather evidence to express assurance on these matters. Accordingly, I do not express an opinion or conclusion on these matters.

## **Predetermined objectives**

22. The annual performance report was not presented for auditing and consequently my findings below are limited to the procedures performed on the strategic planning and performance management documents for the following selected objectives:

- Development objective 2 Basic Services: – pages x to x

23. I assessed the information to determine whether the performance indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the National Treasury's *Framework for managing programme performance information* (FMPPI).

24. The material findings in respect of the selected development objectives are as follows:

## **Development objective 2: Service Delivery (KPA2)**

### **Usefulness of performance information**

25. Performance targets should be specific in clearly identifying the nature and required level of performance as required by the FMPPI. A total of 98% of targets were not specific.
26. Performance targets should be measurable as required by the FMPPI. We could not measure the required performance for 99% of the targets.
27. The period or deadline for delivery of targets should be specified as required by the FMPPI. A total of 100% of targets were not time bound.
28. Performance indicators and measures should be well defined by having clear definitions so that data can be collected consistently and is easy to understand and use, as required by the FMPPI. A total of 64% of the indicators were not well defined.
29. The processes and systems that produced the indicator or measure should be verifiable, as required by the FMPPI. A total of 100% of the indicators and measures were not verifiable.

This was because management did not adhere to the requirements of the FMPPI due to a lack of proper systems and processes.

### **Unaudited supplementary information**

30. The supplementary information set out on pages XX to XX does not form part of the annual performance report and is presented as additional information. I have not audited these schedules and, accordingly, I do not report thereon.

### **Compliance with legislation**

31. I performed procedures to obtain evidence that the municipality had complied with applicable legislation regarding financial matters, financial management and other related matters. My material findings on compliance with specific matters in key legislation, as set out in the general notice issued in terms of the PAA, are as follows:

### **Strategic planning and performance management**

32. The adopted integrated development plan (IDP) did not reflect and identify the key performance indicators and targets and financial plan, as required by sections 26 and 41 of the Municipal Systems Act., as well as Municipal planning and performance management regulation 2(1) and 2(3)(a-c).
33. The municipality did not conduct its affairs in a manner which was consistent with its IDP, as required by section 36 of the Municipal Systems Act., section 21(2)(a) of the MFMA and Municipal planning and performance management regulation 6.
34. The performance management system did not provide for policies and procedures to take steps of improvement where performance targets were not met, as required by section 41 (1)(d) of the Municipal Systems Act.,

35. Measurable performance targets for the financial year were not set in the IDP, for each of the key performance indicators and with regard to each of the development priorities or objectives, as required by section 41(1)(b) of the Municipal Systems Act, and the Municipal planning and performance management regulations 12(1) and 12(2)(e).
36. The annual performance agreements for the municipal manager and all senior managers are not linked to the measurable performance objectives approved with the budget and to the service delivery budget implementation plan as required in terms of section 53(1)(c)(iii) of the MFMA and section 57(1)(b) of the Municipal Systems Act.,.

## **Financial statements, performance and annual reports**

37. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements of non-current assets; current assets; liabilities; revenue and expenditure identified by the auditors in the submitted financial statements were subsequently corrected, but the uncorrected material misstatements and/ or supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.
38. The 2013/14 annual report was not tabled in the municipal council within seven months after the end of the financial year, as required by section 127(2) of the MFMA.

## **Audit committees**

39. An audit committee was not in place, as required by section 166(1) of the MFMA.
40. A performance audit committee was not in place and the audit committee was not used to fulfil the performance audit committee function, as required by Municipal planning and performance management regulation 14(2)(a).

## **Internal audit**

41. The internal audit unit did not function as required by section 165(2) of the MFMA, in that:
42. The internal audit unit did not prepare a risk-based audit plan and an internal audit programme for the financial year under review.
43. Internal audit unit did not report to the audit committee on the implementation of the internal audit plan.
44. The internal audit unit did not advise the accounting officer on matters relating to internal audit, internal controls, accounting procedures and practices, risk and risk management.
45. Sufficient appropriate audit evidence could not be obtained that the internal audit unit advised the accounting officer on matters relating to compliance with the MFMA, the Division of Revenue Act (DoRA) and other applicable legislation, as required by section 165(2)(b)(vii) of the MFMA.

## **Procurement and contract management**

46. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations as required by SCM regulation 17(a) & (c).
47. Quotations were accepted from prospective providers who are not registered on the list of accredited prospective providers and do not meet the listing requirements prescribed by the SCM policy in contravention of SCM regulation 16(b) and 17(b).
48. Goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a).
49. Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM regulation 36(1).
50. Bid specifications were not always drafted by bid specification committees which were composed of one or more officials of the municipality as required by SCM regulation 27(3).

## **Human resource management and compensation**

51. Sufficient appropriate audit evidence could not be obtained that job descriptions were established for all posts in which appointments were made in the current year, as required by section 66(1)(b) of Municipal Systems Act,.
52. The acting corporate service manager was appointed without having met the prescribed minimum competency levels as required by section 56(1)(b) of the Municipal Systems Act.

## **Expenditure management**

53. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
54. Reasonable steps were not taken to prevent unauthorised expenditure, irregular expenditure, fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

## **Conditional grants and transfers**

1. The municipality did not evaluate its performance in respect of programmes or functions funded by the Municipal Systems Improvement Grant allocation, as required by section 12(5) of the DoRA.
2. Sufficient appropriate audit evidence could not be obtained that the Municipal Infrastructure Grant allocation was spent in accordance with the applicable grant framework, in contravention of section 17(1) of the DoRA.
3. The municipality did not evaluate its performance in respect of programmes funded by the Municipal Infrastructure Grant allocation, as required by section 12(5) of the DoRA

## **Revenue management**

4. Interest was not charged on all accounts in arrears, as required by section 64(2)(g) of the MFMA.

## **Asset management**

5. An adequate management, accounting and information system which accounts for assets was not in place, as required by section 63(2)(a) of the MFMA.
6. An effective system of internal control for assets was not always in place, as required by section 63(2)(c) of the MFMA.

## **Consequence management**

7. Unauthorised, Irregular, Fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a)(ii) of the MFMA.
8. Council certified unauthorised, irregular, fruitless and wasteful expenditure as irrecoverable without having conducted an investigation to determine the recoverability of the expenditure, in contravention of section 32(2)(a)(ii) of the MFMA.

## **Internal control**

9. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with legislation. The matters reported below are limited to the significant internal control deficiencies that resulted in a disclaimer opinion, the findings on the annual performance and the findings on compliance with legislation included in this report.

## **Leadership**

10. The leadership did not provide effective leadership based on a culture of honesty, ethical business practices and good governance, protecting and enhancing the interests of the entity. The municipality did not enforce compliance with applicable laws and regulations. And there was no consequence management for those that did not conduct the business of the municipality in line with the rules and regulations.
11. The leadership did not exercise oversight responsibility regarding financial and performance reporting and compliance and related internal controls. Lack of management oversight on preparing, approving and implementing the policies such as fraud prevention, code of conduct, fraud hotline, risk management strategy and draft recruitment policy.
12. The municipality did not implement effective HR management to ensure that adequate and sufficiently skilled resources are in place and that performance is monitored. Financial reporting was given to the external service provider and there was not report for performance information.

13. The leadership did not always have established and communicated policies and procedures to enable and support understanding and execution of internal control objectives, processes and responsibilities.
14. The municipality did not develop and monitor the implementation of action plans to address internal control deficiencies. Internal and audit committee were not effectively used or functional as oversight. Consultants were utilised for the compilation of financial reports, however this is not sufficient to address internal control deficiencies.
15. Establish an IT governance framework that supports and enables the business, delivers value and improves performance.

## **Financial and performance management**

16. There were no proper and effective systems and controls in place as evidenced by:
  - Weekly and monthly reconciliations that were not always adequately prepared for financial items during the year including payroll, taxation, creditors, debtors; and fixed assets. This has resulted in the municipality being required to rely on manual reconciliation at year end. Due to the significant increase in volume of manual reconciliation required, assurance processes were not implemented timely to ensure information is accurate and complete. As a result, a number of errors in the reconciliations were identified by the external auditors.
  - Municipal documents were not always easily accessible when needed.
  - No annual performance report.
17. The municipality did not prepare regularly, accurate and complete financial and performance reports that are supported and evidenced by reliable information. Numerous changes had to be made to the records during the audit and the results of the changes that could not be made resulted in the audit opinion.
18. The municipality did not always review and monitor compliance with applicable legislation.
19. The municipality did not design and implement formal controls over IT systems to ensure the reliability of the systems and the availability, accuracy and protection of information.

## **Governance**

20. The financial and risk unit was not established. The municipality did not conduct risk assessment and did not identify the risks relating to the achievement of the financial and performance reporting objectives. Controls were not always developed to prevent, detect and correct material misstatement in the financial and performance reporting.
21. The internal audit unit did not function as required by section 165(2) of the MFMA and also did not have the guidance from the Audit Committee as it was not established.

22. An audit committee was not in place, as required by section 166(1) of the MFMA. Numerous findings were reported on compliance, financial and performance reporting that could have been minimised by the guidance from the audit committee. The municipality did not utilise the shared services available at the district municipality.

*Auditor General*

30 November 2015



AUDITOR-GENERAL  
SOUTH AFRICA

*Auditing to build public confidence*